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In the Supreme Court of the United States

OCTOBER TERM, 1936

No. 247

EDWARD T. BLAIR, PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF FOR THE RESPONDENT

OPINIONS BELOW

The opinion of the Board of Tax Appeals (R. 90–98) is reported in 31 B. T. A. 1192. The opinion of the Circuit Court of Appeals (R. 107–121) is reported in 83 F. (2d) 655.

The opinions in two earlier proceedings are also involved in the present case. These are *Commissioner* v. *Blair,* 60 F. (2d) 340 (C. C. A. 7th), certiorari denied, 288 U. S. 602, and *Blair* v. *Linn,* 274 Ill. App. 23.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered April 11, 1936 (R. 122). A petition for a rehearing was filed May 1, 1936 (R. 122), and was denied May 27, 1936 (R. 122). The petition for certiorari was filed July 31, 1936, and was granted October 12, 1936 (R. 123). The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

1. Whether the rule of *res judicata* is applicable in this case.

2. Whether specified amounts of income which the petitioner purported to assign to his children, out of income payable to him under a trust created by his father's will, were taxable to the petitioner or to the children.

STATUTES AND REGULATIONS INVOLVED

The statutes and regulations involved are set forth in the Appendix (*infra,* pp. 43–46).

STATEMENT

The facts were stipulated (R. 28–79) and are not in dispute. As found by the Board (R. 80–90), they may be summarized as follows:

The petitioner and another were named trustees of a trust created by the will of William Blair, father of the petitioner (R. 33–42). By the will, the trustees were directed to pay to the deceased's

wife one-half of the net income from the trust property during her lifetime, and to pay the other half to the petitioner during his life. Upon the death of the wife, the whole of the net income was to be paid to the petitioner during his life (R. 37). After the petitioner's death, the income is to be paid to the wife or daughter-in-law of the decedent (petitioner's wife), or to the petitioner's surviving children under certain circumstances, until the youngest child reaches the age of 21. At that time the principal of the trust property is to be transferred to the petitioner's children (R. 38).

The will contained the following provision (R. 83):

> TWENTY: I do hereby declare and direct that the income from said trust fund and estate which is herein ordered to be, from time to time as the same shall be received paid to my said wife and to my said son and to his said wife and to their children and descendants of children in the cases aforesaid shall be paid to them directly upon their separate order and receipt therefor, for their sole and separate use respectively, and that the same shall not be nor be made nor held in any manner nor by any proceedings whether in law or equity while yet in the hands of said trustees liable for or subject to the payment of any of the debts or obligations of either of the persons entitled to the same as above herein set forth.

The wife died in March, 1923. After her death, the petitioner executed and delivered a series of indentures to his children. Each of these provided in substance that the petitioner, in consideration of love and affection and $1, did thereby sell, assign, transfer, and set over to said children "an interest" of specified amounts (in some instances payable annually, in others payable monthly) "in the net income which the * * * [petitioner] now is, or may hereafter be, entitled to receive during his life from the Trustees under the Will of William Blair" (R. 83–84). Each of such indentures authorized and empowered the child "either in her own name or in the name of the said party of the first part [petitioner], to receive and receipt to the Trustees" for the specified amount "in each year thereafter of the income and moneys which shall at any time become payable to" petitioner under the terms of the will of William Blair (R. 84). Each indenture also provided that all payments should be made in person to the particular child and not upon order or assignment, nor by transfer by operation of law, and the assignments were to cease upon the death of either party thereto (R. 84). The trustees, who have, since 1923, been petitioner and his son (R. 85), accepted the assignments and, during the years 1924, 1925, 1926, and 1929, paid to the petitioner's children the sums therein specified out of the income of the trust (R. 86).

In a prior case which involved the petitioner's income tax for the year 1923, the Circuit Court of Appeals for the Seventh Circuit held that the trust here involved was a spendthrift trust and that the income remained taxable to the petitioner despite the assignments. *Commissioner* v. *Blair,* 60 F. (2d) 340, certiorari denied, 288 U. S. 602. (R. 87.) After that decision the trustees (of whom the petitioner is one) filed a complaint in the Superior Court of Cook County, Illinois, naming the petitioner, individually, and the petitioner's children as defendants, reciting the income tax question and the decision of the Circuit Court of Appeals referred to above, and praying the court to construe the will of William Blair and instruct the trustees as to whom they should make payment of the income covered by the assignments. The Superior Court held that the trust was a spendthrift trust and that the assignments in question were invalid. Upon appeal, the Appellate Court of Illinois, First District, with one judge dissenting, reversed the lower court and held that the assignments were valid. *Blair* v. *Linn,* 274 Ill. App. 23. (R. 67–79.)

In the instant case the Board held that notwithstanding the prior decision of the Circuit Court of Appeals it was bound by the decision of the Illinois court, and that under that decision the income paid to the children by the trustees was not taxable to the petitioner (R. 90–98). The Circuit Court of Appeals reversed the Board and held that the assign-

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ments, though valid, were in legal effect merely a direction to pay to the children various specified amounts of the income due to the petitioner, which was not actually payable until it became due and was the petitioner's to dispose of, and that, therefore, such income remained taxable to him (R. 107–121).

SUMMARY OF ARGUMENT

I

The judgment of the Circuit Court of Appeals in *Commissioner* v. *Blair,* 60 F. (2d) 340, is conclusive in this proceeding as *res judicata.* The issue presented in the present case is the same as that already decided in the previous decision. The issue there was whether the petitioner was taxable for the income of the trust created by his father's will although he had executed assignments of that income to his children. That is the very issue now before the Court. The decision of the Illinois Appellate Court in *Blair* v. *Linn,* 274 Ill. App. 23, between different parties, cannot destroy the effect as *res judicata* of the prior decision of the Circuit Court of Appeals between the same parties who are now before the Court.

II

The trust was, under Illinois law, a spendthrift trust. Hence the income therefrom is to be taxed to the beneficiary (petitioner).

A. The judgment of the Illinois court is not controlling in this proceeding. It has long been settled that the only decisions of state courts which are conclusive upon the Federal courts are those of the highest courts of the State, interpreting State statutes or applying a settled rule of property. In the present case the state decision involved is not a decision of the highest court of the State, and it does not interpret a state statute or apply a settled rule of property.

In any event, the decision of the Illinois Appellate Court was not entered until March 31, 1934, many years after the tax years here in question. Regardless of the effect which the Illinois decree may have on payments made thereafter and pursuant to it, it should not be given a retroactive effect so as to alter the legal status of income received and payments already made.

B. The decision of the Illinois Appellate Court is not in accord with the settled law of the State. The will in question contained a comprehensive spendthrift clause which seems plainly sufficient to establish a complete spendthrift trust under the settled law of Illinois. No decision of the Illinois Supreme Court has evidenced the least requirement that any specific phraseology is essential to the creation of a spendthrift trust. Examination of the Illinois cases would seem to make it plain that it is the settled law of the highest court of that State that an instrument containing language

such as that before the Court in the present case results in the creation of a spendthrift trust,—a spendthrift trust which is a bar against voluntary alienation as well as alienation at the suit of creditors.

III

The transactions were assignments of future income and not of a present interest. The court below held that the assignments made by the petitioner were not of a share in the corpus, but only of specific amounts payable out of the income as he received it. This view is supported by the language which this Court used in *Eaton* v. *Boston Safe Deposit & Trust Co.*, 240 U. S. 427, 429, where the restriction against creditors was treated "as limiting the character of the equitable property and inherent in it." If the decision in *Blair* v. *Linn*, 274 Ill. App. 23, must be taken as controlling here, it must be construed, we submit, as a decision that the petitioner's assignments, though valid and effective, were merely orders on the trustee to pay to the children, at stated times, specific amounts out of *his* income. The petitioner's right as a beneficiary of the trust was solely to receive the income *as and when* it should be earned and become due. The income did not become the property of the children assignees except derivatvely, through him. It was his property before it was theirs, just as Earl's income in *Lucas* v. *Earl*, 281 U. S. 111, was his income, and thus taxable to him, before it became

Mrs. Earl's. The statute places the liability for the tax squarely upon the beneficiary.

The petitioner had only future income to assign. As such, the income was attributable to him, and the court below properly held it taxable to him.

ARGUMENT

I

THE JUDGMENT OF THE CIRCUIT COURT OF APPEALS IN *COMMISSIONER* v. *BLAIR*, 60 F. (2D) 340, IS CONCLUSIVE IN THIS PROCEEDING AS *RES JUDICATA*

In *Tait* v. *Western Maryland Ry. Co.*, 289 U. S. 620, this Court decided that the rule of *res judicata* is applicable in income tax cases. That rule, we submit, applies and should be conclusive here. In a prior proceeding between precisely the same parties as are now before this Court, it has been adjudicated that the trust involved in this case is a spendthrift trust, that the purported assignments of income by the beneficiary were invalid, and that the income remained taxable to the petitioner. *Commissioner* v. *Blair*, 60 F. (2d) 340 (C. C. A. 7th); certiorari denied, 288 U. S. 602.

The issue presented in the present case is the same as that already decided in the previous decision. The issue there was whether the petitioner was taxable for the income of the trust created by his father's will although he had executed assignments of that income to his children. That issue has been adjudicated against the petitioner in a previous proceeding between the very parties now

before the Court. Even conceding that the previous Circuit Court of Appeals decision was wrong, and that the decision of the Illinois Appellate Court upon which the petitioner relies shows that it was wrong, nevertheless, the issue has been adjudicated between these parties. That is the essence of *res judicata*. The issue decided in the prior judgment of the Circuit Court of Appeals was the taxability to the petitioner of the income of *this* trust. That is the very issue now before this Court. That there may be new arguments bearing on that issue is, of course, immaterial. The doctrine of *res judicata* seems plainly applicable and controlling here.

So far as the conclusive effect of the prior decision of the Circuit Court of Appeals is concerned, the decision of the Illinois Appellate Court in *Blair* v. *Linn,* 274 Ill. App. 23, seems immaterial. That court merely gave another decision on the same issue which the Circuit Court of Appeals had previously decided. Neither the United States nor the Commissioner of Internal Revenue was a party to the Illinois proceeding. Whatever may be the merits of that decision and its effect on the parties to it, it cannot destroy the effect as *res judicata* of the prior decision of the Circuit Court of Appeals between the same parties who are now before the Court.

It is true that the issue of *res judicata* was not raised by the Government in its answers before the Board of Tax Appeals. This, however, is easily

explainable. The answers were filed on February 15, 1929 (R. 12), and on May 2, 1932 (R. 27). The decision of the Circuit Court of Appeals in *Commissioner* v. *Blair,* 60 F. (2d) 340, was not entered until June 23, 1932, and this Court's denial of certiorari in that case did not occur until February 6, 1933. In other words, the decision upon which the claim of *res judicata* is based was not made until after the Commissioner's answers had been filed with the Board of Tax Appeals. It would doubtless have been better practice to have filed amended answers before the Board. As a matter of fact, neither the taxpayer nor the Government amended its pleadings in any way. The taxpayer's pleadings, for instance, make no reference to the Appellate Court decision entered in 1934.[1] The whole matter was presented to the Board in a somewhat informal way through a Stipulation of Facts (R. 28–79). The Board accepted the case on this basis. However, the Board was not unaware of the prior decision of the Circuit Court of Appeals. It appeared in exhibits which were admitted in evidence (R. 59, 68, 77), it was referred to in the Board's findings of fact (R. 87, 89), and was discussed at great length in the Board's opinion (R. 91, 94). Hence the cases of *United States* v. *Bliss,* 172 U. S.

[1] The decree of the Illinois Appellate Court was not entered until March 5, 1934 (R. 74), and the final decree of the Superior Court of Cook County, in pursuance of the Appellate Court's decision, was entered on March 31, 1934 (R. 76–79).

321, and *Southern Pacific Railroad* v. *United States,* 168 U. S. 1, which dealt with situations in which the decision relied upon was neither pleaded nor in any other way brought to the attention of the court below, are not in point here.

After the taxpayer prevailed before the Board, the Government sought review in the Circuit Court of Appeals. The Government raised the issue of *res judicata* both in its petition for review and in its brief before the Circuit Court of Appeals. The fact of the decision in *Commissioner* v. *Blair,* 60 F. (2d) 340, certiorari denied, 288 U. S. 602, is alleged in the petition for review (R. 101). The fifth and sixth assignments of error in the petition for review were as follows (R. 102):

> 5. The Board erred in holding that it was not required to follow the decision of the Seventh Circuit Court of Appeals in *Commissioner* v. *Blair,* 60 Fed. (2d) 340.
>
> 6. The Board erred in not holding that the question as to whether a spendthrift trust was created was *res adjudicata.*

The *res judicata* issue was argued before the court below, but was not ruled upon by that court.

We submit, therefore, that the rule of *res judicata* is controlling in this case. If this contention is correct it is not necessary to consider the other points raised in this brief.

II

THE TRUST WAS, UNDER ILLINOIS LAW, A SPENDTHRIFT TRUST. HENCE, THE INCOME THEREFROM IS TAXABLE TO THE BENEFICIARY (PETITIONER)

A. THE JUDGMENT OF THE ILLINOIS COURT HOLDING THAT THE TRUST IS NOT A SPENDTHRIFT TRUST, IS NOT CONTROLLING IN THIS PROCEEDING

The petitioner's argument is grounded upon the effect which he contends must be given to the judgment of the Appellate Court of Illinois, entered on March 31, 1934. In the absence of that decision it is clear that the petitioner could not prevail, since the very point was decided against him in *Commissioner* v. *Blair,* 60 F. (2d) 340 (C. C. A. 7th), certiorari denied, 288 U. S. 602.

In considering the effect of the Illinois Appellate Court's decree it must be conceded, of course, that the decree is not binding here on the basis of *res judicata,* since the United States was not and could not have been a party to the proceeding in which it was entered. The question, then, is the possible effect of the subsequent decision of the Illinois Appellate Court.

It has long been settled that the only decisions of state courts which are conclusive upon the Federal courts are those of the highest court of the State interpreting state statutes or applying a settled rule of property. *Irving National Bank* v. *Law,* 9 F. (2d) 536, 537 (C. C. A. 2d); *Westerlund* v. *Black Bear Mining Co.,* 203 Fed. 599, 609 (C. C. A. 8th); *United States Tel. Co.* v. *Central*

Union Tel. Co., 202 Fed. 66, 69 (C. C. A. 6th); *Anglo-American Co.* v. *Lombard,* 132 Fed. 721, 742 (C. C. A. 8th), certiorari denied, 196 U. S. 638. See *Louisville & Nashville R. R. Co.* v. *Garrett,* 231 U. S. 298, 305; *Clarke* v. *Clarke,* 478 U. S. 186, 192; *Pelton* v. *National Bank,* 101 U. S. 143, 144. *Cf. Erie R. R. Co.* v. *Hilt,* 247 U. S. 97; *Ankeney* v. *Hannon,* 147 U. S. 118, 126.

In the present case, the state decision involved is not a decision of the highest court of the State, and it does not interpret a state statute or apply a settled rule of property.

This Court long ago decided that in such a case it is not concluded in the determination of questions presented to it by a state court decision. In *Lane* v. *Vick,* 3 How. 463, the Court construed a will for itself in determining the rights of beneficiaries, although the state court in another proceeding had adopted a different construction. This Court said (p. 476):

> With the greatest respect, it may be proper to say, that this court do not follow the state courts in their construction of a will or any other instrument, as they do in the construction of statutes.
>
> Where, as in the case of *Jackson* v. *Chew,* 12 Wheat., 167, the construction of a will had been settled by the highest courts of the state, and had long been acquiesced in as a rule of property, this court would follow it, because it had become a rule of property.

> The construction of a statute by the Supreme Court of a state is followed, without reference to the interests it may affect, or the parties to the suit in which its construction was involved. *But the mere construction of a will by a state court does not, as the construction of a statute of the state, constitute a rule of decision, for the courts of the United States.* [Italics ours.]

The rules thus announced were approved and applied in many cases, including *Oates* v. *National Bank,* 100 U. S. 239, 246; *Railroad Co.* v. *National Bank,* 102 U. S. 14, 29, 55; *Burgess* v. *Seligman,* 107 U. S. 20, 33–34; and in *Bucher* v. *Cheshire Railroad Co.,* 125 U. S. 555. In *Barber* v. *Pittsburgh, Fort Wayne and Chicago Ry. Co.,* 166 U. S. 83, the controversy related to the construction of a will which had previously been interpreted by the Supreme Court of Pennsylvania. This Court stated the question presented in these words (p. 99):

> The question, whether the opinion of the Supreme Court of the State in the former action is conclusive evidence of the law of Pennsylvania in a court of the United States, depends upon the further question whether the opinion is declaratory of the settled law of Pennsylvania as to the effect of such devises, or is a decision upon the construction of this particular devise.

The court then considered the decision of the Pennsylvania Court, held that it did not represent a

settled rule of property in that State, and concluded that it was not binding in the Federal court.

The principles of these cases were reviewed in detail in *Kuhn* v. *Fairmont Coal Co.*, 215 U. S. 349. And, finally, in *B. & W. Taxi Co.* v. *B. & Y. Taxi Co.*, 276 U. S. 518, the same cases were relied on by this Court in upholding the validity of a contract although the state court had held such contracts invalid. The Court pointed out that the applicable rule was that in the absence of a local statute the Federal courts are free to exercise their independent judgment in the construction of wills, commercial papers, insurance policies, and on other questions of general law.

The principle established by these cases would seem to require the conclusion that the decree of the state court in this case is not conclusive upon this Court in determining the question now before it. No question of the construction and application of a state statute was involved before the Illinois Appellate Court, nor can its decree be considered an application of a settled rule of property in that State. Indeed, as we shall contend below, and as was argued by the dissenting Judge in the Appellate Court (R. 73), the decision of the Appellate Court appears to be quite contrary to the decisions of the Illinois Supreme Court. Under such circumstances, we contend, the decision of the Illinois Appellate Court does not operate to

prevent this Court from considering the question presented on its merits.

The present situation is clearly distinguishable from that which was involved in *Freuler* v. *Helvering,* 291 U. S. 35. That case presented a considerable similarity on its facts to this case; there, as here, the taxpayer relied upon the order of a state court which had construed the trust instrument. This superficial similarity disappears, however, when the *Freuler* case is more closely examined. That case arose under Section 219 (d) of the Revenue Act of 1921 (*infra,* p. 43) which provided that such part of the income of a trust should be taxable to the beneficiary as

> *pursuant to the instrument or order governing the distribution,* is distributable to such beneficiary, whether distributed or not, * * *. [Italics ours.]

The question arose whether certain income was taxable to the beneficiaries, and the beneficiaries relied upon an order of the Superior Court of California which determined that the income should not have been distributed to them. This Court concluded that the California court decision was determinative, saying (pp. 44, 45):

> The word "order" must be given some meaning as applied to trust income which is to be distributed periodically; and we think it clear that the section intended that the order of the court having jurisdiction of the

> trust should be determinative as to what is distributable income for the purpose of division of the tax between the trust and the beneficiary. * * * We think the order of the state court was the order governing the distribution within the meaning of the Act.

It is thus apparent that the decision in the *Freuler* case was induced in large part by the language of the statute involved in that case expressly referring the determination of the taxability of the income to the "order" of the court "governing the distribution." That language, as has been stated, appeared in Section 219 (d) of the Revenue Act of 1921. The present case arises under the Revenue Acts of 1924, 1926, and 1928. None of these Acts contains language similar to that upon which this Court relied in its decision in the *Freuler* case. The corresponding provision of the Revenue Act of 1924 is Section 219 (b) (2) (*infra*, p. 44). There is in that section no reference of any sort to the "order" of the court "governing the distribution." The provision of Section 219 (b) (2) of the Revenue Act of 1926 is the same (*infra*, p. 45). The corresponding provision of the Revenue Act of 1928 is Section 162 (b) (*infra*, p. 45). None of the statutory provisions involved in this case contain any reference to the "order" of any court. In the tax years here involved Congress did not contemplate, as it had in the earlier Act, that the order of a state court should influence the question of

Federal taxation. This Court's decision in *Freuler* v. *Helvering,* 291 U. S. 35, is therefore not controlling here since the statutes here involved do not contain the language upon which the Court there relied.

Indeed, it seems to us that this conclusion must be reached in fairness to the position of the Government in cases of this sort. The Government is largely helpless if its revenues are to be put at the mercy of arrangements substantially *inter partes* in cases like this one. The Government is never made a party in submitting these controversies to the state courts; it could not be made a party. As a matter of fact, it is not ordinarily even notified of the proceeding. In the proceeding before the Illinois courts eventuating in the opinion known as *Blair* v. *Linn,* 274 Ill. App. 23, there was no real dispute between the parties—the present petitioner and his assignees. They were in complete accord and agreement. So far as the parties to the case were concerned, the issue was largely feigned and moot. It was the Government's interest which was substantially affected by the decision, and yet the Government had no day in court, no opportunity to present the arguments opposed to those advanced by the parties before the court. Where, as in the *Freuler* case, Congress has expressly referred the matter to the decision of the state court, then no doubt the Government is bound because Congress has said that it shall be. But here the

statute has been changed; there is no longer any reference in it to the orders of state courts. Unless the Government's rights in these cases are to be put at the mercy of decisions had without allowing it a hearing, the state court decree in this case should not be given a conclusive effect.

Even if the decree of the Illinois Appellate Court might be regarded as conclusive with respect to payments of income made pursuant to it, it cannot have that effect in this case. The tax years which are now before the Court are 1924, 1925, 1926, and 1929. The income in question was received by the trustee and paid out during those years. The final judgment pursuant to the decision of the Illinois Appellate Court was not entered until March 31, 1934 (R. 76–79). It made no adjudication whatever with respect to past payments, either that they had been rightly or wrongly made, and ordered no payment or repayment by anyone on their account. Regardless of the effect which the decree may have on payments made thereafter and pursuant to it, it seems plain that it can have no retroactive effect so as to alter the legal status of income received and payments made many years before the Appellate Court decree was entered. The character and taxability of those payments was fixed when they were made and cannot be altered by a court decision made *ad hoc* and many years later.

B. THE TRUST HERE IN QUESTION WAS, UNDER ILLINOIS LAW, A SPENDTHRIFT TRUST

The will of the petitioner's father creating the trust under which the payments were made contains a very comprehensive spendthrift clause applicable to all the beneficiaries of the trust (R. 83):

> TWENTY: I do hereby declare and direct that the income from said trust fund and estate which is herein ordered to be, from time to time as the same shall be received and paid to my said wife and to my said son and to his said wife and to their children and descendants of children in the cases aforesaid shall be paid to them directly upon their separate order and receipt therefor, for their sole and separate use respectively, and that the same shall not be nor be made nor held in any manner nor by any proceedings whether in law or equity while yet in the hands of said trustees liable for or subject to the payment of any of the debts or obligations of either of the persons entitled to the same as above herein set forth.

Under this clause the income was to be paid to the beneficiaries "directly upon their separate order and receipt therefor, for their sole and separate use respectively," and it was likewise specifically provided that the income should not be subjected to the payment of the beneficiaries' debts through "any proceedings whether in law or equity." It would seem plain that this language

was sufficient to establish a complete spendthrift trust under the settled law of Illinois. No jurisdiction in the United States, except possibly Pennsylvania and Massachusetts, has given the spendthrift trust a more wholehearted reception than has Illinois.[2]

No decision of the Illinois Supreme Court has evidenced the least requirement that any specific phraseology is essential to the creation of a spendthrift trust. Examination of a few of the cases will be sufficient to make this point plain. In *Bennett* v. *Bennett*, 217 Ill. 434, the trust instrument contained no specific words of restraint on alienation. It simply left the sum of $3,000 to a trustee to pay the income to the testator's son until he reached the age of forty years, and then to pay him the principal. Under certain contingencies the principal was not to be paid to the son until he was fifty years of age. In considering this will, the Illinois Supreme Court said (p. 440): "We regard the trust here created and under consideration as what is known as a spendthrift trust, created for the purpose of providing for the maintenance of appellant and at the same time securing it against his improvidence and incapacity for self-protection." And further on in its opinion the court said (p. 442): "The fact that a trustee was appointed and vested with the estate and the bene-

[2] The numerous Illinois cases are reviewed in Griswold, *Spendthrift Trusts* (1936), Secs. 176–178.

ficiary was given the income only is a circumstance from which the intention of the testator to create a spendthrift trust may be inferred." This language was quoted with approval in the Illinois Supreme Court in *Wallace* v. *Foxwell*, 250 Ill. 616, 627–628.

Of particular interest in the present connection is *Wagner* v. *Wagner*, 244 Ill. 101. In this case the court said (p. 111):

> To create a valid spendthrift trust it is not necessary that the *cestui que trust* should be denominated a spendthrift in the will or that the testator should give his reasons for the creation of it. *Nor is it necessary that the will shall in express terms contain all the restrictions and qualifications incident to such trusts.* If, upon a consideration of the will, it appears the intention of the testator was to create such a trust, effect will be given to that intention. [Italics ours.]

This language, too, was quoted with approval in *Wallace* v. *Foxwell*, 250 Ill. 616, 628.

It is true that none of these cases involved the exact question whether the instrument before the court was sufficient to restrain voluntary alienation as well as alienation at the suit of creditors. In view of the sweeping language in the courts' opinions, it seems difficult to doubt that the restraint would have been applicable to both sorts of alienation since both types of restraint are essen-

tial to the full protection of the beneficiary. We are not, however, left in doubt as to the attitude of the Illinois court upon this point. *Hopkinson* v. *Swaim*, 284 Ill. 11, involved a trust the income of which was to be paid to the beneficiaries "directly" (the very word used in the trust instrument in the present case [R. 83]), and which was also "to remain free and exempt from the power and control of any husband and from liabilities for any debts or engagements." There was no express restraint against voluntary alienation. Of this trust the Illinois Supreme Court said (pp. 22–23):

> While the will does not expressly state that the income shall not be subject to alienation by the beneficiary it does state that the income shall be paid to each one directly, which means without the intervention of any medium, agent, or go-between, and not only for her separate use and benefit, free and exempt from the power and control of her husband, but also from liabilities for any debts or engagements. *There could be no such exemption from liability for debt if the beneficiary could convey or assign the income, for if she could do so it could also be seized in execution or attachment or reached by a creditor's bill. The intention of the testator determines the construction of the will, and it is not necessary that a restriction upon alienation shall appear in express terms if the intention is clearly to be gathered from the instrument.* [Italics ours.]

There can be no doubt that the beneficiary's power of voluntary alienation was directly involved in that case and was squarely passed upon by the court. The distinction of that case in the opinion of the Illinois Appellate Court (R. 70) plainly cannot stand in the light of the Supreme Court's language quoted above.

This examination of the Illinois cases would seem to make it plain that it is the settled law of the highest court of that State that an instrument containing language such as that before the Court in the present case results in the creation of a spendthrift trust, a spendthrift trust which is a bar against voluntary alienation as well as against alienation at the suit of creditors.

The same result has been reached by many other courts. In *Shankland's Appeal,* 47 Pa. 113, one of the very early spendthrift trust cases, the will devised property upon trust to pay the income to the beneficiary for his life "without being subject to his debts or liabilities." There was no express restraint against voluntary alienation. The court held that nevertheless the beneficiary did not have power to make a voluntary conveyance of his interest. *Barker's Estate,* 159 Pa. 518, arose over a will providing that the beneficiaries' interests should "be enjoyed by him and them without being in any way subject to or liable for the debts or engagements of my said husband or any of our children." In spite of the absence of a restraint upon volun-

tary alienation, an attempted alienation by a beneficiary was held invalid. See also to the same effect *Welsh's Estate,* 28 Pa. Dist. Rep. 909. A similar result was reached by the Virginia court in *Thomas* v. *House,* 145 Va. 742. Another similar case raising this point is *Jones* v. *Harrison,* 7 F. (2d) 461 (C. C. A. 8th), certiorari denied, *Jones* v. *Ready,* 270 U. S. 652. In that case the will directed that the payments should be made to the beneficiary "direct" (substantially the same word as that used in the present will). The court held that this was sufficient to create a spendthrift trust. The court said (p. 465): "This results from the fact that an estate put in trust, and expressly restricted as to creditors, sufficiently evidences an intent by the testator to impose a restriction also upon the beneficiary's power to alienate or encumber." The previous decision in the present controversy, *Commissioner* v. *Blair,* 60 F. (2d) 340 (C. C. A. 7th), certiorari denied, 288 U. S. 602, is, of course, a square authority to the same effect. See also *King* v. *United States,* 84 F. (2d) 156 (C. C. A. 1st), which is discussed more fully at pp. 31–32 below, and *Croom* v. *Ocala Plumbing & Electric Co.,* 62 Fla. 460.

It should not be overlooked that the interest of the beneficiary of a trust is by statute free from the claims of creditors in Illinois regardless of the terms of the trust. Ill. Rev. Stat. (Smith–Hurd 1935) c. 22, Sec. 49; *Spindle* v. *Shreve,* 111 U. S.

542; *Steib* v. *Whitehead,* 111 Ill. 247. The expressed intention of the settlor to subject the beneficiaries' interests to protective restraints serves no purpose, therefore, unless it is applicable to bar voluntary alienation. The Illinois Appellate Court argued that the testator had complete confidence in the petitioner's business ability and that this circumstance indicated that he did not intend to create a spendthrift trust. (R. 71.) But the petitioner is not the only beneficiary of the trust. His mother, a widow, his wife, and his children, minors at the time, are also beneficiaries. The same spendthrift clause is applicable to all (R. 83). It seems hard to doubt that the testator did intend to establish a complete restraint for the protection of these beneficiaries. The petitioner can hardly contend that this one clause imposes a lesser restraint on him than on the other beneficiaries of the trust.

In the foregoing paragraphs, it has been contended that it is the settled law of Illinois, as well as the uniform conclusion of other decisions which have considered the point, that an express restraint in a trust instrument against alienation at the suit of creditors is sufficient to bar voluntary alienation as well. It is a most significant fact that no other conclusion could be reached if the purpose of protecting the property from the creditors of the beneficiary is to be fulfilled. This follows from the clear provisions of Section

70 (a) (5) of the Bankruptcy Act, c. 541, 30 Stat. 544, 565 (U. S. C., Title 11, Section 110 (a) (5)) which provides in terms that the trustee in bankruptcy is vested with the title of the bankrupt to "property which prior to the filing of the petition he could by any means have transferred * * *." Under this statute if the interest of the petitioner in the present trust is subject to his power of voluntary alienation, then it is property which would pass to his trustee in bankruptcy. If the decision of the Illinois Appellate Court in this case is sound, therefore, the interest of the beneficiary is subject to the claims of creditors upon bankruptcy in spite of the express restraint against the claims of creditors. This is a difficulty which was not considered by the Illinois Appellate Court in its opinion. Perhaps it was not suggested to that court by counsel who were anxious to receive an opinion granting the power of voluntary alienation. Nevertheless, if the decision of the Illinois Appellate Court is correct, the petitioner's interest is subject to the claims of his creditors upon bankruptcy. This seems almost irresistably to show the error of that court's decision, quite apart from its inconsistency with the settled rule established by the decisions of the Supreme Court of Illinois.

This difficulty is clearly shown through a comparison with a decision by this Court which involves a question very closely analogous to that

raised in the present case. This decision is *Eaton* v. *Boston Safe Deposit & Trust Co.*, 240 U. S. 427. This case arose on a writ of error to a decision of the Supreme Judicial Court of Massachusetts, reported as *Boston Safe Deposit & Trust Co.* v. *Luke*, 220 Mass. 484. The will in question provided that the trustee should pay an annuity of $3,000 to the beneficiary, "said income to be free from the interference or control of her creditors." The Massachusetts court held that since a creditor could not reach this income, the trustee in bankruptcy of the beneficiary could not either. In its opinion, the court observed (220 Mass. at 485):

> There is nothing in the will which forbids the life tenant's assigning her equitable life interest. It follows that it was assignable.

This was a clear decision by the state court of last resort that the interest of the beneficiary in question was capable of voluntary alienation in spite of the restraint against the claims of creditors.

The trustee in bankruptcy then carried the case to this Court. The issue thus presented to this Court was extremely similar to that involved in this case. The state court there, as here, had held that the beneficiary's interest was assignable. Should this decision be regarded as conclusive in considering the application of a Federal statute, there the bankruptcy law, here the taxing Acts? The parallel between that case and this is close enough to justify a rather full quotation. This

Court, speaking through Mr. Justice Holmes, said (240 U. S. at 428, 429):

> If it be true without qualification that the bankrupt could have assigned her interest * * * the argument would be very strong that the statute intended the fund to pass. There would be an analogy at least with the provision giving the trustee all powers that the bankrupt might have exercised for her own benefit, Sec. 70 a (3), and there would be difficulty in admitting that a person could have property over which he could exercise all the powers of ownership except to make it liable for his debts. The conclusion that the fund was assignable was based on two cases, and we presume was meant to go no farther than their authority required. The first of these simply held that an executor was not liable on his bond for paying over an annuity to an assignee as it fell due, when the assignor to whom it was bequeathed free from creditors had not attempted to avoid his act. *Ames* v. *Clarke,* 106 Massachusetts, 573. The other case does not go beyond a dictum that carries the principle no farther. *Huntress* v. *Allen,* 195 Massachusetts, 226. It is true that where the restriction has been enforced there generally has been a clause against anticipation, but the present decision in following them holds the restricting clause paramount, and therefore we feel warranted in assuming that the power of alienation will not be pressed to a point inconsistent with the dominant intent of the will.

This Court, therefore, did not follow the Massachusetts decision although it was rendered in the same case and between the same parties, a situation not present here. The decision of this Court seems clearly to have been a decision that the interest in question was not subject to voluntary alienation in spite of the state court's decision that it was. In such light, the case is directly applicable here. In that case, this Court exercised its independent judgment when the application of the Federal Bankruptcy statute was involved. It should similarly exercise its own judgment here where the application of the Federal Revenue Act is in question.

That this is the proper interpretation of this Court's decision in *Eaton* v. *Boston Safe Deposit & Trust Co.*, 240 U. S. 427, is confirmed by a recent decision of the First Circuit Court of Appeals in *King* v. *United States*, 84 F. (2d) 156. That case, as this, involved the taxation of income paid under a trust. It was contended, as here, that the trust instrument restrained only alienation at the suit of creditors and did not invalidate a voluntary assignment executed by the taxpayer. The court held that the decision was controlled by this Court's opinion in *Eaton* v. *Boston Safe Deposit & Trust Co.*, 240 U. S. 427. The court quoted from the opinion of the Massachusetts court in *Boston Safe Deposit & Trust Co.* v. *Luke*, 220 Mass. 484, and then set out substantially the same quotation

from this Court's opinion which has been set forth above. This conclusion was then reached (84 F. (2d) at 159):

> This decision in effect holds that the power of alienation is restricted, not absolute, even where the clause simply provides the "income be free from the interference or control of his creditors." * * *
>
> In view of these decisions of the Massachusetts court and of the Supreme Court of the United States, we conclude that, under the law of Massachusetts, income accruing under a trust containing such provisions as are here shown is made incapable of transfer in anticipation of its accrual by an assignment of the beneficiary.

Under the decision in *Eaton* v. *Boston Safe Deposit & Trust Co.*, the interest of the petitioner in this case would not be held to be assignable if the question arose in the event of his bankruptcy. If his interest is not assignable in that event, it seems difficult to see how it can be regarded as assignable when the controversy arises with respect to taxation rather than with respect to bankruptcy. The petitioner should not be allowed to blow both hot and cold, to have a decision of non-assignability in the event of bankruptcy, and to have a decision of assignability when it will save him income taxes. We submit, therefore, that under the settled law of Illinois and under the decisions of this Court, the interest of the petitioner in this case was not

subject to his voluntary alienation, that the trust here in question was a spendthrift trust, and hence that the income therefrom is properly taxable to petitioner.

III

THE TRANSACTIONS WERE ASSIGNMENTS OF FUTURE INCOME AND NOT OF A PRESENT INTEREST

Petitioner assigned to his children specified amounts to be paid annually out of the net income which he "now is, or may hereafter be, entitled to receive during his life from the Trustees under the Will of William Blair, deceased" (R. 83), and contends that such assigned income is not taxable to him.

The question whether income is taxable to the assignor or to the assignee is found in many decided cases involving different factual situations.[3]

[3] They may be grouped under four headings: (1) Assignment of present or future earnings (*Lucas* v. *Earl*, 281 U. S. 111; *Van Meter* v. *Commissioner*, 61 F. (2d) 817 (C. C. A. 8th); *Hall* v. *Burnet*, 54 F. (2d) 443 (App. D. C.); (2) Assignment of income from property (*Corliss* v. *Bowers*, 281 U. S. 376; *Dickey* v. *Burnet*, 56 F. (2d) 917 (C. C. A. 8th), certiorari denied, 287 U. S. 606); (3) Assignment of contract interests (*Burnet* v. *Leininger*, 285 U. S. 136; *Nelson* v. *Ferguson*, 56 F. (2d) 121 (C. C. A. 3d), certiorari denied, 286 U. S. 565; *Washington* v. *Commissioner*, 80 F. (2d) 829 (C. C. A. 2d); (4) Assignments of income from estates or trusts (*Commissioner* v. *Field*, 42 F. (2d) 820 (C. C. A. 2d); *Helvering* v. *Coxey*, 79 F. (2d) 661 (C. C. A. 3d); *O'Malley-Keyes* v. *Eaton*, 24 F. (2d) 436 (Conn.); *Young* v. *Gnichtel*, 28 F. (2d) 789 (N. J.); *Shellabarger* v. *Commissioner*, 38 F. (2d) 566 (C. C. A. 7th); *Sarther Grocery Co.* v. *Commis-*

In all these cases, the courts have applied, though not always consistently, the general rule that income from personal services is taxable to the one who earns it; that income from property is taxable to the owner or to the one retaining control of the property producing the income, and that any anticipatory arrangement designed in such cases to divert income to another is ineffective to defeat the tax. *Lucas* v. *Earl*, 281 U. S. 111; *Burnet* v. *Leininger*, 285 U. S. 136; *Corliss* v. *Bowers*, 281 U. S. 376.

In the instant case, we have the problem of applying this general rule to the situation where a life beneficiary of the income of a trust purports to assign a part of such income. The petitioner assigned to each of his children "an interest" (of various amounts) in the net income which he was entitled to receive. (R. 83–84.) Such an assignment has been viewed as merely a release of anticipatory income, and not an assignment *in praesenti* of an existing property right (*Wood* v. *Commissioner*, 74 F. (2d) 78 (C. C. A. 6th)); or, as viewed by the court below in the present case, merely a direction to the trustees to pay to his children, out of income due to him, various specified

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sioner, 63 F. (2d) 68 (C. C. A. 7th); *Wood* v. *Commissioner*, 74 F. (2d) 78 (C. C. A. 6th); *Porter* v. *United States*, 52 F. (2d) 1056 (C. Cls.); *Brewster* v. *United States*, 9 F. Supp. 686 (C. Cls.); *Shanley* v. *Bowers*, 81 F. (2d) 13 (C. C. A. 2d); *Lowery* v. *Helvering*, 70 F. (2d) 713 (C. C. A. 2d)).

amounts each year, the theory being that petitioner's right as a beneficiary was solely to receive the income as and when it should be earned and become due and that it was his property before it was theirs, that the income-producing *res* is the *corpus* of the trust and not the beneficiary's right to receive (even though such right is ordinarily treated by equity as creating an interest in the corpus of the trust), and that the assignment by the beneficiary of his right to receive income conveys no part of the income-producing corpus to the assignee.

On the other hand, it has been viewed as an interest presently assignable, like a bond or a building (*Commissioner* v. *Field,* 42 F. (2d) 820 (C. C. A. 2d)), while, in *O'Malley-Keyes* v. *Eaton,* 24 F. (2d) 436 (Conn.), the court held that the assignment of the right to receive income left the assignor without any rights in the trust or its income. See also *Young* v. *Gnichtel,* 28 F. (2d) 789 (N. J.).

The statute itself, we submit, points to the correct solution of the problem. It deals explicitly with the liability of estates or trusts and reveals clearly where Congress intended to impose responsibility for the tax. It provides: " * * * the tax shall be computed upon the net income of the estate or trust, and shall be paid by the fiduciary". (Section 219 (b).) It further provides: "There shall be allowed as an additional deduction in computing the net income of the estate or trust the

amount of the income of the estate or trust for its taxable year which is to be distributed currently by the fiduciary to the beneficiaries * * * but the amount so allowed as a deduction shall be included in computing the net income of the beneficiaries whether distributed to them or not". (Section 219 (b) (2).)

A tax statute is here involved. The import and reasonable construction of the statute are controlling. The statute here is plainly worded. It imposes the liability for the tax on the beneficiary receiving trust income. No liability is placed upon his assignees, and, though they may have enforceable rights against the assignor in courts of equity, the statute points unmistakably to the beneficiary as the one answerable for the tax. No Congressional intent is disclosed to treat the beneficiary's assignee as a beneficiary or a substituted beneficiary. For tax purposes, the petitioner's status as beneficiary is unalterably fixed. Equity may regard the assignment as extinguishing petitioner's rights *in rem* as equitable owner of the trust *res*, or his rights *in personam* against the trustee, but the tax statute, nevertheless, fixes the accountability for the tax upon the petitioner because of his status as beneficiary.

An analogous situation is found in *Burnet* v. *Leininger*, 285 U. S. 136. In that case a husband assigned to his wife one-half of his interest in a partnership and contended that each should return

and pay tax upon one-half of the income attributable to that interest. The taxing Act (Section 218 (a), Revenue Acts of 1918 and 1921) explicitly dealt with the liability of partners as such. This Court said that Congress could and did tax each partner on his distributive share of partnership profits, and held (p. 141):

> In view of the clear provision of the statute, it cannot be said that Leininger was required to pay tax upon only a part of this distributive share because of the assignment to his wife.

An estate or trust is a taxable entity (Section 2 of the Revenue Act of 1924). The fiduciary is responsible for the tax (Section 219 (b), *infra*). Congress, in exercising its authority to tax income, could have imposed the liability for the tax on the fiduciary, without allowing a deduction for distributions of income to beneficiaries. Or it could have relieved the fiduciary of responsibility for the tax on distributions and imposed the liability on the beneficiaries. Congress chose to do the latter. It cannot, therefore, be said that the petitioner is required to pay tax upon only a part of the trust income simply because he made assignments of such income to his children. The statute taxes salaries to those who earn them (*Lucas* v. *Earl, supra*); the statute also taxes partnership income to the individuals carrying on business in partnership (*Burnet* v. *Leininger, supra*). The statute

taxes trust income to the beneficiaries in case of distributions. In all three classes of cases, assignments of income are ineffectual to relieve the assignor from liability for the tax.

The taxpayer in the *Leininger* case urged that the assignment to his wife was of one-half of the "corpus" of his interest in the partnership, and that this "corpus" produced the income in question. This Court stated that that which produced the income was not Mr. Leininger's individual interest in the firm, but the firm enterprise itself; that there was no transfer of the corpus of the partnership property to a new firm, and that her interest in the firm was derivative only, even though the agreement constituted her the beneficial owner of one-half of the income which her husband received from the firm enterprise.

The same considerations are applicable here. The corpus of the trust produced the income in question, not the beneficiary's right to receive it. The agreements with the children amounted to no more than equitable assignments of part of what the petitioner should receive from the trust. The rights of the children were derived from the agreements with their father and rested upon the distributive share which he had and continued to have as a beneficiary of the trust.

Petitioner contends that the children became the beneficial owners of the assigned income. A

similar contention was made in the *Leininger* case, where this Court said (p. 141):

> If it be assumed that Mrs. Leininger became the beneficial owner of one-half of the income which her husband received from the firm enterprise, it is still true that he, and not she, was the member of the firm and that she had only a derivative interest.

So, even if it be assumed that the children became the beneficial owners of part of the income which the father received from the trust, it is still true that he, and not they, was the beneficiary of the trust, and that they had only a derivative interest. The very assignment in this case, as in the *Earl* and *Leininger* cases, was bottomed on the fact that the income would be the petitioner's property, else there would have been nothing on which it could operate. Cf. *Poe* v. *Seaborn,* 282 U. S. 101.

It is, therefore, immaterial whether the law considers an equitable interest for life or for a term of years as present property, alienable like any other. Even though a beneficiary's interest is alienable, as was said in *Commissioner* v. *Field, supra,* assignments of income are ineffective for tax purposes, and this would be true even if the assignments in the present case had manifested an intention to make a present transfer which would extinguish the beneficiary's rights against the trustee and create similar rights in the assignees, enforceable in equity. The cases cited by the peti-

tioner, *Lowery* v. *Helvering,* 70 F. (2d) 713; *Shanley* v. *Bowers,* 81 F. (2d) 13, and *Rossmore* v. *Commissioner,* 76 F. (2d) 520, all from the Second Circuit, follow the *Field* case, which, we submit, was incorrectly decided. There is nothing in the other cases cited by the petitioner which may be construed as permitting the taxation of trust income to any one other than the beneficiary receiving it. The case of *Irwin* v. *Gavit,* 268 U. S. 161, decided that payments received by a beneficiary out of income of a trust is not property acquired by bequest but income taxable in the hands of the beneficiary. This Court said (p. 167): "* * * a gift of the income of a fund ordinarily is treated by equity as creating an interest in the fund", and petitioner relies upon that statement to establish the existence of an assignable interest. It may be freely admitted that the assignments here gave the assignees rights which are enforceable in the courts of the State. The fact remains, however, that the Federal tax statute makes the petitioner, as beneficiary, accountable for the tax on the trust income distributable to him.

We submit that a beneficiary of a trust has only a right *in personam* against the trustee.[4] However, if it be said that a beneficiary's right rises to the dignity of an equitable life estate, corresponding to

[4] See 17 Col. Law Rev. 467, where it is argued that the right of the *cestui* is a right *in personam* against the trustee, specifically enforceable with reference to the trust *res.*

a legal life estate, such a view cannot affect the result here, due to the language of the assignments (R. 83–84):

> That the said party of the first part, * * * does hereby sell, assign, transfer and set over unto said party of the second part an interest * * * *in the net income which the said party of the first part now is, or may hereafter be, entitled to receive* during his life from the Trustees under the Will of William Blair, deceased, * * *. [Italics supplied.]

It is thus clear that here the assignments dealt only with a right to receive the income, and no attempt was made to assign any equitable right, title or interest in the trust itself. The assignments are in substance powers of attorney to receive the income to which the petitioner "may hereafter be entitled." When the assignee collects under these instruments, he does not collect his own income. By the very terms of the instruments he is to collect the income due to the petitioner. This conclusion is fortified by the decision of the Illinois Appellate Court in *Blair* v. *Linn,* 274 Ill. App. 23. If the petitioner is right in his contention that that case is controlling here, he must take the decision in its entirety. That opinion must be construed as a decision that the petitioner's assignments, though valid and effective, were merely orders on the trustee to pay to the children, at stated times, specified amounts out of his income.

It is submitted, therefore, that even if the doctrine of *res judicata* is not applicable and even if the decision of the Illinois Appellate Court may not be ignored, it nevertheless remains true that the assignments here in question did not operate to relieve the petitioner from liability for the tax on the assigned income.

CONCLUSION

The court below reached the correct result; the decision should be affirmed.

Respectfully submitted.

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APPENDIX.

Revenue Act of 1921, c. 136, 42 Stat. 246:

> SEC. 219. (a) That the tax imposed by sections 210 and 211 shall apply to the income of estates or of any kind of property held in trust, including . . . (4) Income which is to be distributed to the beneficiaries periodically, whether or not at regular intervals, and the income collected by a guardian of an infant to be held or distributed as the court may direct.
>
> (d) In cases under paragraph (4) of subdivision (a) . . . the tax shall not be paid by the fiduciary, but there shall be included in computing the net income of each beneficiary that part of the income of the estate or trust for its taxable year which, pursuant to the instrument or order governing the distribution, is distributable to such beneficiary, whether distributed or not, . . .

Revenue Act of 1924, c. 234, 43 Stat. 253:

> SEC. 213. For the purposes of this title, except as otherwise provided in section 233—
>
> (a) The term "gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service * * *, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried

on for gain or profit, or gains or profits and income derived from any source whatever. * * *.

(b) The term "gross income" does not include the following items, which shall be exempt from taxation under this title:

* * * * *

(3) The value of property acquired by gift, bequest, devise, or descent (but the income from such property shall be included in gross income); * * *.

SEC. 219. (a) The tax imposed by Parts I and II of this title shall apply to the income of estates or of any kind of property held in trust, including—

* * * * *

(b) Except as otherwise provided in subdivisions (g) and (h), the tax shall be computed upon the net income of the estate or trust, and shall be paid by the fiduciary. The net income of the estate or trust shall be computed in the same manner and on the same basis as provided in section 212, except that—

* * * * *

(2) There shall be allowed as an additional deduction in computing the net income of the estate or trust the amount of the income of the estate or trust for its taxable year which is to be distributed currently by the fiduciary to the beneficiaries, and the amount of the income collected by a guardian of an infant which is to be held or distributed as the court may direct, but the amount so allowed as a deduction shall be included in computing the net income of the beneficiaries whether distributed to them or not. * * *

The corresponding provisions of Section 213 (a) and (b), and Section 219 (a) and (b), of the Revenue Act of 1926 are identical with the foregoing; and the corresponding provisions of Section 22 (a) and (b), and Section 162 (b), of the Revenue Act of 1928 are substantially the same.

Treasury Regulations 65, promulgated under the Revenue Act of 1924:

> ART. 73. *Gifts and bequests.*—Property received as a gift, or received under a will or under statutes of descent and distribution, is exempt from the income tax, although the income therefrom derived from investment, sale, or otherwise is not. * * *
>
> ART. 342. *Method of computation of net income and tax.*—The statute provides that the tax computed upon the net income of the estate or trust shall be paid by the fiduciary, except in the case of the trusts described in article 347. However, in computing the net income of the estate or trust, the following deductions will be allowed either in addition to, or in lieu of (as the case may be) those specified in section 214 in the case of individuals:
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> * * * * *
>
> (2) The amount of the income of the estate or trust for its taxable year which is to be distributed currently by the fiduciary to the beneficiaries, and the amount of the income collected by a guardian of an infant which is to be held or distributed as the court may direct, shall be allowed as an additional deduction in computing the net income of the estate or trust. The amount so allowed as a deduction must be included by a beneficiary in computing his net income, whether distributed to him or not. If the

> taxable year of the beneficiary differs from that of the estate or trust, the amount which he is required to include in computing his net income shall be based upon the income of the estate or trust for its taxable year ending within his taxable year. * * *

The corresponding provisions of Articles 73 and 342 of Regulations 69, relating to the Revenue Act of 1926, are identical with the foregoing; and the corresponding provisions of Articles 83 and 862 of Regulations 74, relating to the Revenue Act of 1928, are substantially the same.

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